Mason, Monte

From: Jack King [jckkng@mcn.net]
Sent: Thursday, August 04, 2005 9:18 AM
To: Mason, Monte
Cc: Montana Petroleum Association
Subject: Royalty increase memo to Monte

HANCOCK ENTERPRISES
MEMO FROM JACK E. KING

POB 2527 BILLINGS MT. 59103 jckkng@mcn.net 406-252-0576 406-252-1760 fax

August 3, 2005

To: Monte Mason, Minerals Management Bureau Chief
Re: Royalty Rate Review

Monte:

I am the manager for a Montana, family owned, oil and gas exploration company that has been in business in Montana for over 60 years. I am also the chairman of the lands committee for the Montana Petroleum Association, and member of the Montana Board of Oil and Gas Conservation Commission. However, I am writing this primarily from my perspective, as I have been unable to reach a consensus among M.P.A."s members, which is understandable.

The lack of consensus is indicative of how a one-size fits all royalty affects different sized operators in different geologic areas exploring for a variety of targets with a variety of economics. The companies operating exclusively in the Williston Basin Bakken play have tempered objections to the proposal. Independents operating outside the Williston Basin have uniformly advanced strong criticism toward a royalty increase well above the standard they currently pay to fee owners.

The independent's concerns are well founded based upon our company's personal experience, as we are one of the larger private mineral owners in the Rockies including Montana. Our experience is the only place in Montana we can get a royalty of 1/6th or more for our minerals is in very selective areas of the Williston Basin. The rest of the State has a typical royalty rate of less than $1/6^{th}$ for fee leases.

Independents, including individual geologists and landmen drive the exploration efforts in this State. The Bakken play was kicked off by an independent. They require lower royalty rates to make their personal economics work when they raise capital to get their prospects drilled. Often, with their only reward being a retained overriding royalty for their efforts risk and expense. These independents avoid developing new prospects in areas where royalties exceed a certain level.

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ITEMS TO CONSIDER

Raising royalty rates will decrease bonuses and rentals received by the State.

Fewer leases will be nominated and consequently evaluated and explored.

State royalty increases will trigger requests for higher fee royalty triggering a cycle of less activity in Montana. (Until recently we were unable to sell any Montana prospects, as companies did not even have a MT geologist, because the climate was too onerous. This royalty combined with the other oppressive items being advanced will kill much of the progress we have made in MT over the last 6 years.)

Montana is the **only State** to have significant increases in oil and gas production over the last two years. The system is working. Leave it alone.

State rules and regulations on State leases have multiple onerous regulatory issues attached to them, relative to fee leases.

State annual rentals are higher than typical fee leases.

New lease plays typically have lower fee royalties. The State is now included in those plays which rarely see fruition or production. They would be excluded if the royalty were set at 1/6th.

Any increase in tax or royalty will cause the premature abandonment of all wells as they enter the "stripper" phase of their production.

Tribal lands are mentioned as receiving excess royalty in the "Dear interested Party" report. I think tribal lands activity or lack thereof is a good example of what can happen to leasing, exploration and production levels when the regulatory and economic environments are not competitive, and the combination of requirements, royalty and regulations squeeze the incentive for doing exploration.

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As you can read I think it would be a mistake for the State to increase its royalty rate. But as the famous economist Yogi Berra said, "don't make the wrong mistake". If the Land Board feels compelled to increase the royalty, please consider an option tagged to the bonus paid for a lease. The bonus is an indicator of the quality of the prospect and its potential economics.

BONUS	ROYATY RATE
$25 or less	no change
$25.25-$55	15%

$55.25+	16.67%

Thank you for your review of the foregoing. Please call if you have any questions.

Jack E. King

RECEIVED
AUG 0 8 2005
D.N.R.C.

Frederick S. Johnson
Wyoming Professional Geologist #1589
4330 South Oak Street
P. O. Box 232
Casper WY 82602
August 5, 2005

Mr. Monte Mason
Montana DNRC
P. O. Box 201601
Helena MT 59620-1601

Re: Suggested Royalty Rate Increase on Oil and Gas

Dear Sir:

In reference to your request for comments on Royalty Rate Review, the following is my observations after over forty years in the exploration business in Montana, Wyoming, North Dakota and Colorado, where I have enjoyed production income from all states mentioned.

Many of the discoveries of the past have been initiated by independent geologists who sold their ideas in the form of purchased leases to larger companies. Most of mine went to major oil companies, or sometimes, large independents.

Where a mineral royalty is higher than those in surrounding areas, companies have not allowed me to keep royalty on these leases. In the past, it has been difficult to ask much in the way of up front monetary returns of any consequence for leases. Only the establishment of hydrocarbon production could one expect a decent return. With the larger royalty, I would be cut out of royalty on a state lease (as happened in Wyoming to me). Therefore, there is little incentive for me to buy a Wyoming state lease, where often I'd pay a rental or two prior to a decent market. So I learned only to buy leases around the state lease, or if it took up a substantial portion of the prospect, I would go elsewhere. Wyoming lost the money I would have paid, plus the rentals during slow times, whether or not there was any production. (I can name for you many tracts where they lost money)

One geologist with a big company, if the market is hot, and a large potential, could make Montana more money with a larger royalty on a given lease. But many small geologists, with proper incentives, can make the state money in rentals, even though many are dry holes or not drilled. More prospects drilled from more ideas would bring a much greater return also, even with a smaller royalty.

In the past, Montana has developed a bad reputation for environmental excesses, tax or royalty problems, and other things I may not even be aware of. One company told me they would not look at a prospect in Montana, and some did reluctantly, but did not buy. I have several good prospects I would like to see drilled in Montana, having lived there and worked the area for years. But I am reluctant to do anything because of the reputation this great state is getting. A higher royalty may be just another nail in the coffin.

With 1/6 royalty, if prices are high enough, companies would still buy state leases with high potential, but with slow times and other problems, as we have seen, reluctance is there.

Very truly yours,

Frederick S. Johnson

Frederick S. Johnson, Geologist

Canyon Natural Gas, L.L.C.
P.O. Box 183 Phone: 406-245-3810
Billings, MT 59103 Fax: 406-245-3810

August 11, 2005

Monte Mason
Montana DNRC
P.O. Box 201601
Helena, MT 59620-1601

Via Email: mmason@mt.gov

Dear Mr. Mason:

Thank you for notice of the State's consideration to raise the lease royalty rate and the invitation to comment. In addition to being a taxpayer my qualification to comment is some 15+ years experience in the oil and gas exploration industry spanning a twenty-five year period.

I am against the proposed increase in current form. First, the State increase, any increase, is by definition a disincentive to those who plan, develop, and generate capitol and production. The increase from 12.5% to 16.667% is roughly a 33% increase with no underlying economic rational other than the fact that the State "can". To that extent the increase is confiscatory.

In addition, if the increase is being considered retroactively, this is nothing short of arbitrary and a major business deterrent. The results could very well have a negative impact on State revenue.

Secondly, the increase does not measure up when analyzed with other competing states. Yes, other states have a $1/6^{th}$ royalty. North Dakota did and then repealed it when they found it to be a disincentive. But the other states, like Wyoming, have far less production taxes. When added to the existing tax structure a producer might pay 29% in tax and royalty, and that is without federal tax. That's too much actually and comparatively.

Thirdly, the proposal is ill conceived from a tactical perspective. If the State views itself as a participant and steward of mineral resources it would want to cooperate with explorationists in distinguishing prospects as to success probability or risk/reward. In other words some acreage is high-risk wildcat, some developmental or low risk. Wildcat leases should provide the highest incentive to reward the risk. Yet the State's proposal would not make such a distinction thereby creating an inefficient variable for producers to have to account for in prospect analysis.

Finally, I strongly urge the Land Board, at the very least, to consider allowing further time, study and comment period prior to making a decision to increase the royalty to this extent and having such a major impact on the revenue and perception of Montana throughout the oil and gas industry and business environment.

Sincerely,

Michael Okerman, Member

Canyon Natural Gas, L.L.C.

RANCK OIL COMPANY INC.
P.O. Box 548
Cut Bank, Montana 59427
Phone 406-873-2591
FAX 406-873-2598

RECEIVED
AUG 09 2005
D.N.R.C.

August 4, 2005

CERTIFIED MAIL

Department of Natural Resources and Conservation
Trust Land Management Division
Monte Mason, Chief
P. O. Box 201601
Helena, MT 59620-1601

RE: Oil and Gas Lease Application
Township 28 North, Range 5 West, MPM
Section 16: ALL
Pondera County, Montana

Dear Mr. Mason:

Please be advised that we hereby withdraw application number 5023 for Pondera County, Montana submitted on June 9, 2005 for the next state lease sale on September 7, 2005. This leases is in "stripper well" territory and any increase from the 12.5% royalty to the state, as indicated in recent communications received from your department, would likely makes this lease uneconomical. Although current oil prices are in excess of $50.00 per barrel when you consider the production taxes imposed by the state and add an increase the royalty rate the current well on the location is uneconomical. Therefore, we shall make arrangements to have the well bore on this lease plugged.

Since we made the application with the tacit understanding that the lease would provide for the traditional 12.5% royalty to the state, we are requesting the refund of the application fees made to the state.

Sincerely,

Barbara J Ranck Perry

Barbara J. Ranck-Perry
President

Reger

OIL REAL ESTATE INVESTMENTS

Memo from James R. Reger, Reger Oil, LLC
To: Monte Mason, Minerals Management Chief

August 9, 2005

Monte:

I am the managing partner of an Oil and Gas Exploration Co. I disagree with the department's idea of a single royalty rate.

I think that the DNRC staff should go back to the drawing board By only giving the Land Board a few options, is nonsense.

Wildcat acreage is very speculative. No one gives more then 1/8 (12.5%) in wildcat areas. Geologic and geophysical information is non existent on most areas, not near production. Wells are expensive to drill. 1 out of 50 is the percentage of successful wells in wildcat areas. These areas need incentives to get the wells drilled. If the well is successful, the area around the new well can revert to a higher royalty rate because it is now in a known oil producing area.

The people that are telling you to raise the rate, don't drill wildcat oil wells. They take no risks. Leave the wildcat areas to the wildcatters. Give us an incentive to spend $500,000.00 to $ 1 Million per well.

Remember, they raised the Coal Severance tax and no one came to mine coal in Montana, they went to Wyoming, where the tax was lower.

James R. Reger

REGER OIL
P.O. BOX 1782 BILLINGS, MONTANA 59103
BUS: 406-248-3139 CELL: 406-698-1010 FAX: 406-248-5344 E-MAIL: Reger3@bresnan.net

Robert A. Schalla
Independent/Consulting Geologist
7314 Charolais Street
Billings, Montana 59106
(406) 656-1647

RECEIVED
AUG 1 0 2005
D.N.R.C.

August 8, 2005

Mr. Monte Mason
Montana DNRC
P.O. Box 201601
Helena, MT 59620-1601

Dear Mr. Mason:

I am writing in response to your request for comments from interested parties regarding the proposed changes to oil and gas leases on State lands in Montana.

In my view the proposed royalty rate increase, which is in effect merely an increase in the tax rate on the oil and gas industry in Montana, is potentially very dangerous. I realize it is always appealing to attempt to increase State revenues by raising taxes on industries which are doing well, or appear to reaping "windfalls" from their current business activities, the negative affect of these tax increases often is not obvious or immediately apparent.

The **revenue-negative** affects of the proposed royalty increase include, but are not limited to, an immediate reduction in lease bonus bids and over time, a decrease in exploratory drilling on State lands.

The reason that total bonus payments are certain to fall is that much of the leasing activity in Montana is generated by independent geologists, like myself, and small promoter-type companies that do not have the wherewithal to conduct actual exploration drilling. These entities generate prospects on State lands with the expectation that they will be able to attach a reasonable over-riding royalty interest to the lease to compensate them for their time and effort should a discovery be made. If the proposed royalty increase is implemented independents and promoters will have much lower incentives to pursue prospects on State lands, bidding competition at sales will therefore decrease, as will overall exploration activity because fewer prospects will be generated. Larger companies will also decrease their maximum bid levels, based on the decreased Net Present Value of possible reserves. In this regard it should be remembered that bonus payments are "cash-in-hand" to the State treasury, whereas royalties may or may not ever generate any revenue.

Although I firmly believe that the proposed royalty increases are a bad idea I would like to suggest some compromise solutions based on my experience exploring for oil and natural gas in Montana and the surrounding states.

1) An increased royalty could be imposed on State lands, which are located in the immediate vicinity of existing production. The inclusion area could be any lease which lies within a one mile radius circle of a currently producing well. The rationale being that proximity to production gives the lease increased value.

2) If the Land Commissioners are absolutely committed to increasing the royalty on ALL State lands, then consideration should be given to a system similar to Wyoming, where State leases are still available with 12.5% royalty if they receive no bids at a given sale. These leases are then made available as an "over-the-counter" (no bonus payment) filing if they receive no bids at a second lease sale.

Thank you for your consideration of these proposals.

Sincerely,

Robert A. Schalla

Monte Mason

RECEIVED
AUG 0 9 2005
D.N.R.C.

Dear Sir

8/5/05

My comment is, that its very bad timing, with fuel Costs already high.

Fred Skierka
Skierka Bro Inc

Fred Skierka
HCR 78 Box 14
Chester Mt 59522

CHESTER, MT
PM
AUG 8
2005
59522

Monte Mason
Montana DNRC
P O Box 201601
Helena Mt
59620-1601

Request For Comments

STONE ENERGY

MICHAEL E. CUBA
Denver District Manager

Stone Energy Corp.
Suite 2600
950 17th Street
Denver, Colorado 80202
Telephone: (303) 685-8000
Fax: (303) 296-4075

August 12, 2005

Monte Mason
Montana Department of Natural Resources
1625 11th Avenue
Helena, MT 59620

Re: State of Montana Royalty Rates

Via Email: mmason@mt.gov
And Overnight Mail

Dear Mr. Mason:

Stone Energy Corporation hereby submits comments for the State of Montana's consideration in regards to possibly raising royalty rates as to State lands. Stone does not support this proposal.

Please be advised that Stone is presently very active in the State with three drilling rigs running fulltime within Montana. We anticipate our operations will add substantial revenue to the State through existing royalties on State of Montana leases, the State share of federal royalties and various taxes. In addition, we are also providing employment for numerous individuals and our activities have a multiplying benefit to the State as each of our suppliers and service companies have employees that spend money thus improving the economy of the State while also generating ever-increasing tax revenues.

Stone recently commenced operations in Montana upon making a substantial property acquisition at a considerable cost and intends to be a very good corporate citizen. Stone entered the State under a reasonable assumption that State royalty rates would continue at the present levels and had significant plans to participate in State of Montana oil and gas lease sales. Again, Stone does not support the proposal for increased royalty rates on State lands as such an increase would have a negative effect on our economics resulting in lower amounts and fewer bids on State leases. This could lead to less activity within the State. I encourage you to take a look at the big picture of the benefits the oil and gas industry already brings to Montana and that you not raise your rates at a time when such activity is at a highpoint. Careful not to shoot the goose that bears the "black" golden eggs.

As you know, many of the oil and gas plays in Montana also exist in North Dakota where the royalty on State lands is below the level you are considering for Montana. And the neighboring State of Wyoming has a more attractive business climate when State royalties and various taxes are considered together. The oil and gas business is very competitive and economically sensitive. Your action could drive business away to a more fiscally reasonable state and essentially backfire.

We suggest the Land Board not move hastily in the direction of higher royalties on State of Montana lands and take adequate time to study the matter carefully. It is our belief that you will find it most beneficial to the State and to the hard-working risk-taking companies and individuals that produce oil and gas within the State to **not** raise royalty rates.

Thank you very much for the opportunity to provide comment.

Very truly yours,

Michael E. Cuba
Denver District Manager

ZIER & ASSOCIATES, LTD.
A Professional Land Services Agency • Right of Way, Due Diligence, Oil, Gas & Minerals

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AUG 11 2005
D.N.R.C.

August 9, 2005

Department of Natural Resources & Conservation
State Land Board
POB 201601
Helena, MT 59620-1601

Re: Royalty Rate on State of Montana Oil & Gas Leases
August 15, 2005 Board Meeting

Sirs:

I hope I am not too late to put in a comment on the proposed royalty increase in State leases. We have conducted numerous wildcat lease programs for various clients in the past 5-6 years assembling blocks in excess of 150,000 acres.

It is my thought that a 1/6th royalty rate on wildcat lands is too heavy and might affect State leasing. I believe that on wildcat leases, the rate should remain the same.

For leases in close proximity to production, however, an increased royalty rate is probably warranted. I do know that North Dakota has such a statue and have operated very successfully with it. I've not seen their statute, but I believe it fluctuates depending upon production with a lesser royalty rate on marginal wells.

Thank you for the opportunity to comment.

Yours very truly,

Nancy C. Zier

POB 1834 • Billings, MT 59103-1834 • *Office:* 1-406-256-6592 • *Cell:* 1-406-698-5867 • *Fax:* 1-406-252-3265 • *Email:* nancyczier@msn.com

Mason, Monte

From: David Knapp [dknapp@midrivers.com]

Sent: Thursday, August 11, 2005 7:33 PM

To: Mason, Monte

Subject: Royalty Rate Review Comment

Monte:

I know I am getting this in just under the wire, but I thought it was worth sending, because based on what I read in the report, it is an angle on the different royalty option that may not have been considered.

The comment would be that the board consider an option whereby leases that are nominated for a sale, but are not competitively bid on at the sale and go to the applicant, would be issued with the current royalty rates and any leases that did receive competitive bidding, would be issued with the 1/6th royalty rate.

It would seem to me that this would not be that hard to administer and would more fairly reflect activity levels, commodity prices and generate more income from the trust lands, because of more lands being nominated in highly speculative areas, that odds are won't produce anyway.

Thank you for your consideration.

David Knapp
Sidney, Montana

Mason, Monte

From: Smyers, Larry [LSmyers@fortunaenergy.com]

Sent: Tuesday, August 09, 2005 7:19 AM

To: Mason, Monte

Subject: Royalty rate survey

Dear Mr. Mason:
I have downloaded your Royalty Rate Review paper and it coincides with an internal survey I have been tasked with. I am surveying royalty rates for federal, state and private

rates in the producing states and have reached some dead ends, especially in the eastern states. I would appreciate it if you could share websites or contacts where some of the royalty rates are available. The federal is fairly straight forward, however the state by state and private sectors are more difficult. I am also making a comparison of the amount of state land owned versus the amount under oil and gas leases. I would also appreciate knowing if there is a source for this data. I would enjoy visiting with you and possibly there is some data that I have useful to you.

Sincerely,
Larry Smyers
607-795-2769

Larry F. Smyers

Mason, Monte

From: Robin Trudell [lefselady@hotmail.com]

Sent: Thursday, August 11, 2005 10:22 AM

To: Mason, Monte

Subject: comments on royalty rates

Royalty rate increase for oil and gas leases on state school trust land is long overdue!

The royalty rate on leases in Richland County has been 1/6th or higher for several years.

This observation comes from spending 20 plus years on the board of directors of the Northeast Montana Land and Mineral Owners Association.

Dennis Trudell